

Chapter 6

INVESTMENTS OF THE FUND

General

- 6.01 The fund's assets must be relevant and consistent with the investment objective of the fund.
- 6.02 Reasonable steps must be taken to ensure that, taking into account the investment objective and policy of the fund, the fund's assets provide a prudent spread of risk.

Dealings in the fund's assets

- 6.03 All dealings in the fund's assets must be appropriate to the fund and consistent with the securities laws, these Guidelines, prospectus and deed.
- 6.04 The fund manager must–
- (a) inform the trustee in writing of any acquisition or disposal of a fund's assets within one business day after which the acquisition or disposal was effected;
 - (b) ensure that the fund's assets have adequate proof of title or ownership to allow proper custodial arrangements to be made; and
 - (c) cancel a transaction or make a corresponding acquisition or disposal at its own expense to secure restoration of the previous position where the trustee conveyed an opinion that a particular acquisition or disposal exceeds the powers conferred on it, or is otherwise contrary to the interests of the unit holders.

Investment powers: General

- 6.05 The fund's assets may only consist, unless otherwise provided in these Guidelines, of the following:
- (a) Transferable securities;
 - (b) Money market instruments;
 - (c) Deposits with financial institutions;
 - (d) Units or shares in CIS;
 - (e) Derivatives; and
 - (f) Securities other than (a) and (d), and investment accounts other than (b). For the purposes of these Guidelines, these financial instruments are referred to as 'other securities'.
- 6.06 A fund may not acquire any asset or engage in any transaction which involves the assumption of any liability which is unlimited.
- 6.07 Transferable securities and money market instruments held by the fund must be traded or dealt in or under the rules of an eligible market. Transferable securities that are not traded or dealt in or under the rules of an eligible market is permitted subject to the exposure limit stipulated in Schedule B of these Guidelines.

Investments in transferable securities

6.08 Transferable securities refer to—

- (a) shares or securities equivalent to shares;
- (b) bonds or other forms of securitised debt; and
- (c) sukuk,

but do not include money market instruments or any security where the title can be transferred only with the consent of a third party.

6.09 Transferable securities must meet the following criteria:

- (a) The maximum potential loss which the fund may incur as a result of the investment is limited to the amount paid for it;
- (b) The investment is liquid, and will not impair the fund's ability to satisfy its redemption and other payment commitments;
- (c) The investment is subject to reliable and verifiable valuation on a daily basis; and
- (d) There is appropriate information available to the market on the investment.

6.10 For avoidance of doubt, shares that are not listed and quoted on a stock exchange but have been approved by the relevant regulatory authority for such listing and quotation, and are offered directly to the fund by the issuer, will be deemed to

be transferable securities traded or dealt in or under the rules of an eligible market.

Investments in CIS

6.11 A fund may invest in other CIS that fall within the following categories:

- (a) A CIS authorised or recognised by the SC; or
- (b) A CIS that meets the following criteria:
 - (i) The CIS is constituted and regulated in a jurisdiction where the laws and practices provide the level of investor protection that is at least equivalent to that offered in Malaysia;
 - (ii) The rules on investments, borrowing and lending are substantially similar to the requirements in these Guidelines. This would exclude hedge funds;
 - (iii) The assets of the CIS are managed by an entity which is approved, authorised or licensed by a securities regulator to conduct fund management activities; and
 - (iv) The business of the CIS is reported in half-yearly and annual reports to enable an assessment to be made of the assets and liabilities, income and operations over the reporting period; or
- (c) A CIS that meets the following criteria:

- (i) The CIS invests in permissible investments under paragraph 6.05(a) to (e), physically-backed metal ETF that comply with paragraph 6.12, or real estate;
 - (ii) The CIS meets the criteria imposed on transferable securities as prescribed under paragraph 6.09;
 - (iii) The units or shares in the CIS are listed for quotation and traded on a stock exchange that is an eligible market; and
 - (iv) The CIS is not an inverse or leveraged product; or
- (d) A CIS that does not comply with paragraphs 6.11(a), (b) or (c), but subject to the exposure limit stipulated in Schedule B of these Guidelines.

6.12 Where a fund invests in a physically-backed metal ETF, the physically-backed metal ETF must meet the following criteria:

- (a) The assets of the physically-backed metal ETF, i.e. the physical metal, is held in trust and is segregated from the assets of the manager, sponsor, trustee or custodian; and
- (b) The physically-backed metal ETF adopts a passive management strategy with the objective of tracking the price of the metal.

6.13 Where the fund invests in a CIS operated by the same management company or its related corporation, the fund manager must ensure that–

- (a) there is no cross-holding between the fund and the CIS;
- (b) all initial charges on the CIS is waived; and
- (c) the management fee must only be charged once, either at the fund or the CIS.

Investments in derivatives

- 6.14 The fund's assets may consist of derivatives that are either listed or quoted on a stock exchange, or dealt in the OTC market, provided that the fund's global exposure from derivatives position does not exceed the fund's NAV at all times. The global exposure may be calculated using the approach described in Part 1, Appendix I of this Chapter after taking into account the fund's investment strategy, the types and complexities of the derivatives used, and the proportion of the fund's portfolio which comprise derivative instruments.
- 6.15 The underlying instruments of a derivative must only consist of permissible investments under paragraph 6.05 and may also include commodities, indices, interest rates and foreign exchange rates. Where the underlying instrument of a derivative is a commodity, such derivative must be settled in cash at all times and this must be set out in the deed and prospectus.

6.16 The derivative must meet the following criteria:

- (a) The derivative must be liquid and will not impair the fund's ability to satisfy its redemption and other payment commitments;
- (b) The exposure to the underlying assets of the derivative must not exceed the investment restrictions or limitations applicable to such underlying assets and investments as set out in Schedule B of these Guidelines;
- (c) The derivative is subject to reliable and verifiable valuation on a daily basis;
- (d) The derivative can be sold, liquidated or closed by an offsetting transaction at any time at its fair value; and
- (e) The derivative must not result in the delivery of investments other than those prescribed under paragraphs 6.05(a) to (d).

6.17 In the case of OTC derivatives, reliable and verifiable valuation pursuant to paragraph 6.16(c) refers to the following:

- (a) A valuation made by the management company based on a current market value; or
- (b) Where such value is not available, a fair value based on an appropriate valuation method which is checked at an appropriate frequency by an independent party.

Embedded derivatives

- 6.18 Where a transferable security or money market instrument embeds a derivative, the requirements in paragraphs 6.14 to 6.17 and 6.23 apply to the embedded derivative.
- 6.19 Where the counterparty risk of the embedded derivative is or may be transferred to the fund, paragraphs 6.24 and 6.25 also apply to the embedded derivative.
- 6.20 A transferable security or money market instrument is considered to be embedding a derivative if it contains a component that fulfils the following criteria:
- (a) The component results in some or all of the cash flows that otherwise would be required by the transferable security or money market instrument which functions as a host contract to be modified according to a variable including but not limited to a specified interest rate, price of a financial instrument, foreign exchange rate, index of prices or rates, credit rating or credit index, and therefore vary in a way similar to a standalone derivative;
 - (b) The component's economic characteristics and risks are not closely related to the economic characteristics and risks of the host contract; and
 - (c) The component has a significant impact on the risk profile and pricing of the transferable security or money market instrument.
- 6.21 A transferable security or a money market instrument should not be regarded as embedding a derivative where it contains a component which is contractually transferable

independently of the transferable security or money market instrument. Such a component should be deemed to be a separate financial instrument.

- 6.22 Where an instrument is structured as an alternative to an OTC derivative or tailor-made to meet the specific needs of a fund, the instrument must be deemed as embedding a derivative.

Cover

- 6.23 The management company must ensure the fund is able to meet its payment and delivery obligations incurred under transactions in derivative, whether for hedging or for investment purposes, at all times.

OTC derivatives

- 6.24 The OTC derivative must meet the following:
- (a) The counterparty of an OTC derivative must be a financial institution with a minimum long-term credit rating of investment grade (including gradation and subcategories); and
 - (b) Subject to the aggregate limit in Schedule B of these Guidelines, the maximum exposure of a fund to the counterparty, calculated based on the method as described in Part 2, Appendix 1 of this Chapter, must not exceed 10% of the fund's NAV.
- 6.25 For the purpose of paragraph 6.24(a), where the rating of the counterparty falls below the minimum required, or the counterparty ceases to be rated, the fund manager should, within six months or sooner, if the trustee considers it to be

in the best interest of the unit holders, take the necessary action to ensure that the requirements are complied with.

Investments in deposits

6.26 The fund's assets may consist of placement of deposits provided that it is with a financial institution.

Investments in other securities

6.27 Investment in other securities is subject to an exposure limit stipulated in Schedule B of these Guidelines.

6.28 The fund manager must ensure that there are appropriate policies and procedures for the valuation of the other securities as well as have in place the necessary risk management policy and procedures to enable it to monitor, measure and manage the risks relating to the investment and their contribution to the overall risk profile of the fund.

Securities lending and repurchase transactions

6.29 The fund may undertake securities lending and repurchase transactions provided that these are for the sole purpose of efficient portfolio management. A transaction is deemed to be for the purpose of efficient portfolio management if it meets the following criteria:

- (a) Economically appropriate and realised in a cost-effective way;
- (b) Entered into for one or more of the following specific aims:
 - (i) Reduction of risk;

- (ii) Reduction of cost; or
 - (iii) Generation of additional capital or income for the fund with a level of risk which is consistent with the risk profile of the fund and the risk diversification requirements as prescribed in these Guidelines;
- (c) The exposure is fully covered to meet any obligation to pay or deliver; and
 - (d) The risks are adequately captured by the risk management policy and procedures of the fund.
- 6.30 The fund manager must ensure that it has appropriate policies and practices for the lending of securities and repurchase transactions by the fund. The fund manager must ensure that the volume of securities lending or repurchase transactions is kept at an appropriate level.
- 6.31 For the purpose of securities lending, a fund may lend its transferable securities either–
- (a) directly;
 - (b) through a standardised lending system facilitated by a clearing house which performs a central counterparty role; or
 - (c) through securities lending agents, who are recognised as specialists in securities lending.
- 6.32 Securities lending and repurchase transactions must be effected in accordance with good market practice.

- 6.33 The fund manager must have at least 100% collateralisation in respect of the securities lending and repurchase transactions into which it enters and ensure there is no uncollateralised counterparty risk exposure arising from these transactions. The collateral must meet the requirements in Appendix II of this Chapter.
- 6.34 All the revenues arising from securities lending and repurchase transactions, net of direct and indirect expenses as reasonable and normal compensation for the services rendered in the context of the securities lending and repurchase transactions, must be returned to the fund.
- 6.35 The securities lending and repurchase transactions must be permitted under the deed and disclosed in the prospectus.

Counterparty

- 6.36 The counterparty to the securities lending and repurchase transactions must be a financial institution that has a minimum top three long-term credit rating (including gradation and subcategories) provided by any Malaysian or global rating agency.
- 6.37 Where the counterparty to the securities lending and repurchase transactions is a party related to the management company or the fund manager, the management company or the fund manager, as the case may be, must have adequate arrangements in place to manage potential conflict of interests.
- 6.38 The agreement between the fund and the counterparty, either directly or through its agent, must require the counterparty to provide additional collateral to the fund or its agent no later than the close of the next business day if

the current value of the eligible collateral tendered is insufficient.

- 6.39 Except otherwise provided under paragraph 6.29, the fund's assets may not be lent. In addition, the fund may not assume, guarantee, endorse or otherwise become directly or contingently liable for, or in connection with, any obligation or indebtedness of any person.

Borrowings

- 6.40 Except otherwise provided under paragraph 6.29, the fund is prohibited from borrowing other assets (including borrowing of securities within the meaning of Securities Borrowing and Lending Guidelines) in connection with its activities.
- 6.41 Notwithstanding paragraph 6.40, the fund may borrow cash for the purpose of meeting repurchase requests for units and for short-term bridging requirements.
- 6.42 For the purpose of paragraph 6.41, the management company must ensure that—
- (a) the fund's cash borrowing is only on a temporary basis and that the borrowings are not persistent;
 - (b) the borrowing period must not exceed one month;
 - (c) the aggregate borrowings of a fund must not exceed 10% of the fund's NAV at the time the borrowing is incurred; and
 - (d) the fund only borrows from financial institutions.

Investment Limits

- 6.43 The fund manager must ensure that the investment limits and restrictions set out in Schedule B of these Guidelines are complied with at all times based on the most up-to-date value of the fund's assets.
- 6.44 The limits and restrictions in Schedule B do not apply to securities or instruments issued or guaranteed by the Malaysian government or Bank Negara Malaysia.
- 6.45 In determining compliance with the limits or restrictions, any accrued entitlement on the securities or instruments held by the fund may be excluded. The entitlement should not be exercised if the exercise results in a breach of any limit or restriction.
- 6.46 Although the limits and restrictions under Schedule B of these Guidelines apply only on a per fund basis, the fund manager is encouraged to have prudential internal limits and restrictions on a group-of-funds basis if the funds are operated by the same management company.

Breach of investment limits

- 6.47 The management company must notify the SC, within seven business days, of any breach of investment limits and restrictions in this Chapter with the steps taken to rectify and prevent such breach from recurring.
- 6.48 Notwithstanding paragraph 6.47, any breach as a result of any –
 - (a) appreciation or depreciation in value of the fund's investments;

- (b) repurchase of units or payment made out of the fund;
- (c) change in capital of a corporation in which the fund has invested in; or
- (d) downgrade in or cessation of a credit rating,

need not be reported to the SC but must be rectified as soon as practicable within three months from the date of the breach unless otherwise specified in these Guidelines.

- 6.49 Notwithstanding paragraph 6.48, the three-month period may be extended if it is in the best interest of unit holders and trustee's consent is obtained. Such extension must be subject to at least a monthly review by the trustee.

Voting rights

- 6.50 The fund manager or the trustee is encouraged to exercise the voting rights for any share held by the fund at a shareholder meeting of corporations whose shares are so held.